JUN 28 1941
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Supreme Court of the United States

OCTOBER TERM 1941.

No. 220

FREDA R. CASPERSEN, *Petitioner*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

AND

BRIEF IN SUPPORT THEREOF

JACKSON R. COLLINS,
Counsel for Petitioner.

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Supreme Court of the United States

October Term 1941.

Docket No. --------

FREDA R. CASPERSEN, *Petitioner*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

MAY IT PLEASE THE COURT:

The petitioner, Freda R. Caspersen, by her attorney, Jackson R. Collins, respectfully shows to this Honorable Court:

A.

Summary Statement of the Matter Involved

The case involves alleged deficiencies in federal income taxes of the petitioner for the calendar years 1934 and 1935 in the amounts of $1,369.51 and $1,406.03 respectively.

The deficiencies result from a determination by the Commissioner of Internal Revenue that *all of* the income of a

trust created by the petitioner was taxable to her as the grantor under Section 167 of the Revenue Act of 1934, c. 277, 46 Stat. 680, 26 U. S. C. A. Int. Rev. Acts, P. 727, because the balance of the trust income in excess of the payments made to the grantor was distributable to her "in the discretion of * * * (a) person not having a substantial adverse interest in the disposition of such part of the income." The United States Board of Tax Appeals held that the husband-trustee had a substantial adverse interest and ruled for the petitioner. The United States Circuit Court of Appeals for the Third Circuit reversed the decision of the United States Board of Tax Appeals, holding that the husband-trustee had no substantial adverse interest. The majority opinion was written by Judge Jones; Judge Maris dissented.

The questions involved are as follows:

1. Does a husband-trustee to whom property is irrevocably conveyed, with sole and absolute discretion to distribute or accumulate the income therefrom in such divisions and proportions as he might designate to his needy relatives and other relatives named in the trust instrument as he might appoint, consisting of the grantor, their minor son, his aged parents, her aged parents, aunts and other relatives of the husband-trustee and grantor, have a substantial adverse interest in the disposition of such income to that of the grantor?

2. Is Section 167 (a) (2) of the Revenue Act of 1934 constitutional if construed to permit the taxation to the grantor of income of a trust which was neither distributed to nor accumulated for her, nor applied nor applicable to the discharge of any of her obligations, and the distribution of which was not subject to her control?

The material facts are as follows:

Taxpayer, a resident of New Jersey, on June 3, 1932, transferred to her husband, Olaus W. Caspersen, as trustee,

certain shares of stock having a value of about $55,000 in trust, the trust agreement providing in part that:

> (3) From the net quarterly income arising from the trust fund hereby created, to pay FIRSTLY, to the said Freda R. Caspersen for and during such time as the said Olaus W. Caspersen, her said husband, shall live, the sum of Six hundred ($600.00) dollars every three months, provided, however, that she shall during such time remain the wife of the said Olaus W. Caspersen, and SECONDLY, to pay out of the remaining balance, after the aforesaid payment, to any blood relative or relatives of the said Freda R. Caspersen and Olaus W. Caspersen at such time, in such amounts, and to such person as in the sole judgment of said Trustee, Olaus W. Caspersen, he shall choose and deem best or proper, to aid them in meeting their necessary living expenses, and THIRDLY, and unexpended income remaining after the aforesaid payments in the discretion of and during trusteeship of Olaus W. Caspersen may be paid in whole or in part to the said Freda R. Caspersen or if not paid at the close of the calendar year, shall FOURTHLY, be added to the corpus of the trust and shall be reflected in a special account on the books of the trust. Such amount as may be accumulated as evidenced by this account may be distributed in the discretion of Olaus W. Caspersen, during his trusteeship only, for the payment of educational, food, shelter, clothes, medical or other necessary expenses of any child or children of Olaus W. Caspersen and Freda R. Caspersen or any issue of such child (R. 1, 2).

Numerous contingencies and final distribution of the trust fund were provided for in the trust instrument. The trust was not to end until both the taxpayer and her husband had died and their son had attained the age of 40 years, or sooner died, but the husband-trustee had power to terminate the trust during his life, in which case the trust fund was to be distributed to the children of taxpayer and her husband or to the issue of such children. The trust has not been terminated. Some of the shares of stock trans-

ferred in trust taxpayer had purchased and the rest she had received as a gift from her husband (R. 2).

The income of the trust was (R. 3):

Year	*Income*	*Non-taxable long term capital gains*	*To grantor*	*To needy blood relatives (1)*	*Accumulations*
1934	$ 9,522.30	—	$5,200	$ 895.27	$3,427.07
1935	10,482.12	$395.32	3,400	2,720.19	4,756.95

Those relatives in 1934 included taxpayer's mother, her trustee-husband's niece and two needy aunts, two aunts of the trustee-husband's father and an aunt of his mother; and in 1935, also the mother of the husband of the taxpayer and his cousin. All of them were old and not wealthy. None of the accumulated income has been paid to or on behalf of the son. The trust has not loaned or borrowed money (R. 2, 3).

The taxpayer included within her taxable income only the amounts actually distributed to her (R. 3).

The United States Board of Tax Appeals ruled that the husband had a substantial adverse interest in the disposition of trust income because it enabled him without hindrance or accountability to use the income for the discharge of his own obligations to support his minor child as he is required by New Jersey law; the need to support his mother and other relatives was not mentioned in its opinion though set forth in the record and the brief on behalf of the taxpayer. The United States Board of Tax Appeals held that

---

(1)

Name	*1934*	*1935*
Rose Budson, mother of taxpayer	$350.00	$ 350.00
Rose Westby, aunt of trustee	400.00	—
Annette Andreassen, aunt of trustee	20.00	130.00
Christiana Sivertsen, Aunt of trustee's father	50.00	100.00
Mary Sivertsen, aunt of trustee's father	50.00	100.00
Alma Caspersen, aunt of trustee	12.93	—
Thea Tollittson, aunt of mother of trustee	12.30	15.09
Esther Simonson, cousin of trustee	—	25.00
Augusta Caspersen, mother of trustee	—	2,000.00
Totals	$895.23	$2,720.09

this was not remotely possible a legal or contingent obligation, but that it was a presently existing obligation inherent in the fact that the child was a minor and without sufficient means of support and maintenance. The Board held that the power to use any income for the support of his child gave the husband such a substantial adverse interest in it as to support a disregard of the financial position of the wife and refusal of any demand or request which she might make for the income in regard to its use. *In New Jersey a mother has no obligation to support her child if the father is able to do so.* Here the father was quite able and did support the child. The Board held that this was an interest adverse to that of the grantor irrespective of a common interest in the welfare of the child and their apparently harmonious relations (R. 3, 4).

The United States Circuit Court of Appeals for the Third Circuit reversed the decision of the United States Board of Tax Appeals. The Court held that the adverse interest of the husband-trustee based on his duty to support his child was offset by his duty to support his wife. They further held that the grantor was under a similar duty to support the child without quoting authority (either case or statutory) which alleged rule was erroneous and contrary to the long established New Jersey rule that the wife or mother has not such duty as long as the husband-father is able to do so. The Court decided that these factors offset the duty of the husband-trustee and that he had no substantial adverse interest under Section 167 (a) (2) of the Revenue Act of 1934 (R. 7-13). In the language of this Court they sought to determine what they thought the law of New Jersey ought to be rather than what it was. *Klaxon* v. *Stentor,* decided June 2, 1941, No. 741, reported in *The United States Law Week* for June 3, 1941, Vol. 9, Sec. 4, page 4380.

B.

Reasons Relied on for the Allowance of the Writ

I.

In recent years there has been a great development of legislation to minimize and alleviate absolute poverty and want in this country. Social Security Laws, Unemployment Compensation Laws, Workmen's Compensation Laws and Old Age Assistance Laws are a few of the recent statutes. Under the laws of New Jersey a man is liable to support his minor child; he is also required to support blood relatives as set forth in Title 44, Article 17 of *New Jersey Statutes, Annotated.*[1] If he should fail to do so, he may be forced to by the courts.

Moreover, every civic and every Christian rule imposed this adverse economic duty upon the husband-trustee. The finding and declaring such duty as not substantially adverse violates the cherished ideals and duties of the American family. To find and declare that there is no substantial adverse legal interest is to degrade and undermine respect for the Courts, because the good people of the land know such a rule of law undermines and destroys the foundations and institutions of America. The issue is of fundamental importance, regardless of correcting the injustice to this particular taxpayer.

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[1] "*Relatives chargeable*

The father, grandfather, mother, grandmother, children, grandchildren, and husband or wife, severally and respectively, of a poor, old, blind, lame or impotent person or other poor person or child not able to work, shall, if of sufficient ability, at his or their charge and expense, relieve and maintain the poor person or child in such manner as the overseer of the poor shall order, or the court upon its own initiative or the information of any person, after notice to the person or persons chargeable and hearing the overseer, may so order."

There is a moral obligation and a natural impulse for a man to apply any fund that is a surplus above all duties in accordance with his station in life to the support of his children and other old and "needy" relatives, (most of whom were more than 70 years of age and the amounts distributed were the difference between existence and living).

In fact and in law the husband-trustee in this case had an adverse substantial interest in the trust fund. This Honorable Court has never settled the question as to what is a substantial adverse interest of a trustee, husband or son, or nephew. The statutes of New Jersey and applicable principles in Social Security Laws indicate that the United States Circuit Court of Appeals for the Third Circuit erred in holding that the husband-trustee had no substantial adverse interest; and to hold that he had no such interest departs so far from the accepted and usual course of judicial procedures as to call for the exercise of the power of supervision by this Honorable Court.

Sound family relationship and its duties are paramount to immediate collection of revenue, and in the long run develop true administrative efficiency. They are here presented in direct form.

II.

The taxpayer did not receive the income for which the Commissioner has assessed deficiencies; said income discharged no obligation of the taxpayer or its equivalence, and it will never be available to her. To tax her on this income is to require her to pay tax upon the income of another. Such taxation results in the taking of property without due process of law and is in violation of the Fifth Amendment.

Wherefore, petitioner respectfully prays that a Writ of Certiorari be issued out of and under the seal of this

Honorable Court directed to the United States Circuit Court of Appeals for the Third Circuit, demanding that Court to certify and send to this Court, for its review and determination on a day certain therein to be named, a full and complete transcript of the record and all proceedings in this case numbered and entitled on its docket "No. 7450, *Commissioner of Internal Revenue* v. *Freda R. Caspersen,*" and that said judgment of the United States Circuit Court of Appeals for the Third Circuit may be reviewed by this Honorable Court, and that this petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

JACKSON R. COLLINS,
Counsel for Petitioner.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI

I.

The Opinions of the Courts Below

The opinion of the United States Circuit Court of Appeals for the Third Circuit was rendered on April 1, 1941. It is reported in 119 F. (2d) 94, and is to be found on pages 7 to 13 of the record herein.

The opinion of the United States Board of Tax Appeals is reported in (1940) 40 B. T. A. 758, and appears on pages 1 to 5 of the record herein.

II.

Jurisdiction

1. The statutory provision believed to sustain jurisdiction is Section 240 of the Judicial Code as amended by the Act of February 13, 1925 (c. 229, sec. 1; 43 Stat. 938).

2. The judgments sought to be reviewed were entered on April 1, 1941 (R. 13).

3. The proceeding in which review was sought was initiated in the United States Board of Tax Appeals. It involves the liability of the petitioner for income taxes under section 167 (a) (2) of the Revenue Act of 1934 on income of a trust created by her. The United States Board of Tax Appeals found for the petitioner and against the government and denied the deficiency assessments. Upon petition for review, the United States Circuit Court of Appeals for the Third Circuit reversed the United States Board of Tax Appeals and entered judgment for the Commissioner of Internal Revenue.

III.

Statement of the Case

A full statement of the case has been given under heading "A" in the petition and in the interest of brevity is not repeated.

IV.

Specification of Errors

The United States Circuit Court of Appeals for the Third Circuit erred in the following respects:

1. In holding that Olaus W. Caspersen, the trustee under the deed of trust involved in this proceeding and the husband of the petitioner, had no interest in the disposition of the income of said trust substantially adverse to that of the petitioner because it erroneously applied the laws of the State of New Jersey.

2. In failing to determine that section 167 (a) (2) of the Revenue Act of 1934 is unconstitutional if construed to require the taxing as petitioner's income of income of said trust, the distribution of which was not subject to her control and no part of which was distributed to nor accumulated for her nor applied nor applicable to the discharge of her obligations, where it is not necessary to prevent tax evasion, nor is there an equivalence.

V.

ARGUMENT

POINT I

Olaus W. Caspersen, the husband-trustee, was possessed of a substantial adverse interest in the disposition of the trust income in question.

The principal question presented is whether Olaus W. Caspersen, trustee and husband of the petitioner, had an interest substantially adverse to the petitioner in the disposition of the trust income.

Section 167 of the Revenue Act of 1934, 48 Stat. 729, 26 U. S. C. A. 167, provides:

> "(a) Where any part of the income of a trust
>
> (2) may, in the discretion of the grantor or of any person not having a substantial adverse interest in the disposition of such part of the income, be distributed to the grantor:
>
> then such part of the income of the trust shall be included in computing the net income of the grantor."

It is the contention of the petitioner that her husband, Olaus W. Caspersen, possessed a substantial adverse interest within the intendment of the statute. The husband-trustee had a legal duty to support their minor child; he also had a duty to support *his* blood relatives as required by New Jersey law and permitted by the trust instrument.

This Honorable Court has decided that the federal courts cannot set up an independent federal, general or common law except

> "in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State . . . There is no federal

> general common law . . . And no clause in the Constitution purports to confer such a power upon the federal courts." *Erie Railroad Company* v. *Tompkins,* (1938) 304 U. S. 64, 58 S. Ct. 817.

The federal courts are not entitled to decide what state law *ought* to be, they must determine what the state law *actually is. Klaxon* v. *Stentor,* decided June 2, 1941, No. 741, reported in *The United States Law Week* for June 3, 1941, Vol. 9, Sec. 4, page 4380.

The United States Board of Tax Appeals held that the trustee had a substantial adverse interest in the trust because of his duty to support the child. The United States Circuit Court of Appeals for the Third Circuit reversed this decision on the grounds that the mother had a similar duty.

Under New Jersey law the mother of a minor child is liable to support that child, *only* where the father fails to do so. The duty of support rests primarily on the father; it is only in the event that he cannot do so that the mother is liable for such support. New Jersey law goes far in imposing the duty of support of minor children on the "man" of the family. It even holds that

> "The provision of this section (imposing duty of support) shall apply to the minor children of a mother whose husband shall fail properly to support and maintain such children when by reason thereof they are likely to become a public charge upon the municipality in which they have gained a legal settlement." *New Jersey Statutes Annotated, Title* 44:1-140.

See also *In re Ganey,* (1921) 93 N. J. Eq. 389, 116 Atl. 19; *Alling* v. *Alling* (1894) 52 N. J. Eq. 92, 27 Atl. 655.

Therefore, the United States Circuit Court of Appeals for the Third Circuit erred in holding that the husband-trustee had no substantial adverse interest in the trust because of his duty to support the child, as the mother was

also liable. The Court misinterpreted the New Jersey law and disregarded the rule that the father is solely liable, the mother being liable only in the event that the father fails. The federal courts cannot interpret state law by what they believe it should be; they must interpret state law as it is. *Klaxon* v. *Stentor*, decided June 2, 1941, No. 741, reported in *The United States Law Week* for June 3, 1941, Vol. 9, Sec. 4, page 4380.

Moreover, the United States Circuit Court of Appeals for the Third Circuit did not consider whether the duty of the trustee to support his mother and other blood relatives as required by New Jersey law was a substantial adverse interest.

> "The father, grandfather, mother, grandmother, children, grandchildren, and husband or wife, severally and respectively, of a poor, old, blind, lame or impotent person or other poor person or child not able to work, shall, if of sufficient ability, at his or their charge and expense, relieve and maintain the poor person or child in such manner as the overseer of the poor shall order, or the court upon its own initiative or the information of any person, after notice to the person or persons chargeable and hearing the overseer, may so order." *New Jersey Statutes Annotated*, Title 44:1-140.

The settlor was under no legal duty to support the mother of the husband-trustee, as there was no blood relationship between them as required by the New Jersey statute. On the other hand, not only did the husband-trustee have a legal duty to do so, but also, acting under the provisions of the trust, he did support his mother from the trust income. It cannot be held, therefore, that the husband-trustee had no substantial adverse interest in the trust because of his duty to support his mother on the grounds that a settlor of the trust had a similar duty; in fact and in law the settlor had no duty to support the blood relatives of her husband. In so holding the United States Circuit Court of

Appeals for the Third Circuit erred in its determination of the law of New Jersey.

> "There may always be exceptional cases or particular circumstances which will prompt a reviewing or appellate court, where injustice might otherwise result, to consider questions of law which were neither pressed nor passed upon by the court or administrative agency below. *Hormel* v. *Helvering*, Law Ed. Advance Opinions, rendered March 31, 1941, Vol. 85, page 651 at 654.

But this is not a fresh issue raised for the first time in this petition; it was presented before the United States Board of Tax Appeals and the United States Circuit Court of Appeals for the Third Circuit. This point was made in the brief below and orally presented in the argument before the Court.

Congress has not defined the term "substantial adverse interest" as used in the statute. The Congressional purpose, however, was to block a possible means of tax avoidance by the device of vesting the power to distribute the income in some person having no stake in the trust or a stake so insubstantial that the holder of the power would not improbably be amenable to the grantor's wishes. (*Fulham* v. *Commissioner*, (1940) 110 F. (2d) 916).

The statute is aimed at immorality. A situation truly condemned and sought to be reached by it can only arise where the grantor, ostensibly relinquishing the right to income, chooses someone as trustee who will acquiesce in his wishes to the end that he may, in fact, receive or retain that which apparently he is giving away. The statute is not aimed at a trust created for a legitimate purpose.

Whether a trust falls within the scope of the statute must be determined upon an appraisal of the trust instrument against a background of realities (*Fulham* v. *Commissioner*, supra); in the light of the settlor's intention in creating the trust and the course of conduct subsequent

to its creation (*Commissioner* v. *Morton*, (1940) 108 F. 2d) 1005; *Henry A. B. Dunning*, (1937) 36 B. T. A. 1222; *Raoul H. Fleischmann* v. *Commissioner*, (1939) 40 B. T. A. 672.

POINT II

Section 167 (a) (2) of the Revenue Act of 1934 is unconstitutional if it be construed to require taxation to the grantor of trust income which is neither distributed to nor accumulated for her nor applied nor applicable to the discharge of her obligations, and the distribution of which is not subject to her control, because it is not necessary to prevent tax evasion, nor is there an equivalence.

Congress has the power to adopt means fairly and reasonably calculated to prevent the avoidance of taxation. Nevertheless, the provisions of the statute adopted may be so arbitrary and capricious as to amount to confiscation and thereby offend the Fifth Amendment to the Constitution (*Heiner* v. *Donnan*, (1932) 285 U. S. 312, 52 S. Ct. 358). There are limits to the power of Congress to create a fictitious status under the guise of supposed necessity (*Helvering* v. *City Bank Farmers Trust Co.*, (1935) 296 U. S. 85, 36 S. Ct. 70). It is not necessary to tax the petitioner here to prevent tax avoidance.

A tax may be levied where the person called upon to pay the tax received a benefit substantially similar to a benefit received by other persons who are within the scope of the normal operation of the same tax statute, but where there is no equivalence the "lawmakers have done a wholly arbitrary thing" and "laid a burden unrelated to privilege or benefit" (*Burnett* v. *Wells*, (1933) 289 U. S. 670, 53 S. Ct. 761).

The effect of this statute, if applied to the petitioner, would be to find "equivalence where there was none nor anything approaching it" and to lay "a burden unrelated to privilege or benefit" (*Burnett* v. *Wells*, supra).

The decision of the Supreme Court in *Hoeper* v. *Tax Commission*, (1931) 284 U. S. 206, 52 S. Ct. 120, holding a statute unconstitutional which attempted to levy a tax on a husband, based upon the combined income of both husband and wife, points to the unconstitutionality of Section 167 (a) (2) if construed to compel taxation to the petitioners of income of the trust actually distributed to others. To the same effect are *Schlesinger* v. *Wisconsin*, (1926) 270 U. S. 230, 46 S. Ct. 260, and *Bowers* v. *Kerbaugh-Empire Co.*, (1926) 271 U. S. 170, 46 S. Ct. 449, and the dissenting opinion in *Charles H. Mott* v. *Commissioner*, (1934) 30 B. T. A. 1040.

CONCLUSION

It is respectfully submitted that this case calls for the exercise by this Court of its supervisory powers in order that the construction and constitutionality of the federal statutes involved be definitely determined and the errors of the Circuit Court of Appeals for the Third Circuit in determining the laws of New Jersey be corrected, and that, to such end, writ of certiorari should be granted and the court should review the decision of the United States Circuit Court of Appeals for the Third Circuit and finally reverse it.

Dated, June 26, 1941.

JACKSON R. COLLINS
Counsel for Petitioner

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In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 220

FREDA R. CASPERSEN, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 1–5) is reported in 40 B. T. A. 758. The opinion and dissenting opinion in the Circuit Court of Appeals (R. 7–13) are reported in 119 F. (2d) 94.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered April 1, 1941 (R. 13). The petition

for a writ of certiorari was filed June 28, 1941. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The taxpayer transferred property to her husband in trust to pay a specified amount of income annually to herself, the remaining income to be distributed, in the husband's discretion, to the taxpayer, or to relatives of either of them, and any income still remaining to be accumulated for the benefit of their son. Is the taxpayer accountable for the income in excess of that actually paid to her? The answer depends upon whether her husband had a "substantial adverse interest" in the disposition of such remaining income within the meaning of Section 167 of the Revenue Act of 1934.

STATUTE AND REGULATIONS INVOLVED

The statute and regulations are set forth in the Appendix, *infra,* pp. 9–12.

STATEMENT

The Board of Tax Appeals found the following facts (R. 1–3):

Taxpayer, a resident of New Jersey, on June 3, 1932, transferred to her husband, Olaus W. Caspersen, as trustee, certain shares of stock having a value of about $55,000 in trust, the trust agreement providing in part (R. 1–2) that—

(3) From the net quarterly income arising from the trust fund hereby created, to pay Firstly, to the said Freda R. Caspersen for and during such time as the said Olaus W. Caspersen, her said husband, shall live, the sum of Six hundred ($600.00) dollars every three months, provided, however, that she shall during such time remain the wife of the said Olaus W. Caspersen, and Secondly, to pay out of the remaining balance, after the aforesaid payment, to any blood relative or relatives of the said Freda R. Caspersen and Olaus W. Caspersen at such time, in such amounts, and to such person as in the sole judgment of said Trustee, Olaus W. Caspersen, he shall choose and deem best or proper, to aid them in meeting their necessary living expenses, and Thirdly, any unexpended income remaining after the aforesaid payments in the discretion of and during trusteeship of Olaus W. Caspersen may be paid in whole or in part to the said Freda R. Caspersen or if not paid at the close of the calendar year, shall Fourthly, be added to the corpus of the trust and shall be reflected in a special account on the books of the trust. Such amount as may be accumulated as evidenced by this account may be distributed in the discretion of Olaus W. Caspersen, during his trusteeship only, for the payment of educational, food, shelter, clothes, medical or other necessary expenses of any child or children of Olaus W. Caspersen and Freda R. Caspersen or any issue of such child.

Numerous contingencies and final distribution of the trust fund were provided for in the trust instrument. The trust was not to end until both the taxpayer and her husband had died and their son had attained the age of 40 years, or sooner died, but the husband had power to terminate the trust during his life, in which case the trust fund was to be distributed to the children of taxpayer and her husband or to the issue of such children. The trust has not been terminated. Some of the shares of stock transferred in trust taxpayer had purchased and the rest she had received as a gift from her husband (R. 2).

The taxpayer and her husband live together. They have one son now living, who was born in January 1929. He had a few thousand dollars' worth of property in his own name in 1935. Taxpayer's husband created a trust of which the son is a beneficiary. Taxpayer also set up another trust for the son. The son is the beneficiary of a life insurance policy. Taxpayer's husband opened a bank account for the son; she and her husband made gifts to him of $25 each month, and these were deposited in the account (R. 2).

The income of the 1932 trust was $9,522.30 in 1934 and $10,482.12 in 1935. Of this, $5,200 was distributed to taxpayer in 1934 and $3,400 in 1935; approximately $3,400 was added to the corpus in 1934 and $4,756.95 in 1935, and the balance in each year was distributed to blood relatives of taxpayer

and her husband. Those relatives in 1934 included taxpayer's mother, and her husband's niece, two aunts, two aunts of his father and an aunt of his mother; and in 1935, also the mother of taxpayer's husband and his cousin. Most of them were old and not wealthy. None of the accumulated income has been paid to or on behalf of the son. The trust has not loaned or borrowed money. (R. 2–3.)

In the years 1932–1935 taxpayer's husband had gross and net income as follows (R. 3):

	Gross income	Net income
1932	$43,742.58	$41,407.00
1933	41,225.32	37,301.61
1934	43,137.81	40,782.06
1935	54,432.76	51,786.00

In 1932 he had approximately $100,000 in assets. In 1934 he paid for a governess who took care of the son. He owns a house in Montclair, New Jersey, for which he paid approximately $14,000 or $15,000, and he maintains it as a home. He pays all the bills in connection with its upkeep and maintenance and supports his wife and son according to their station in life (R. 3).

The taxpayer included within her taxable income for 1934 and 1935 only the amounts of the trust income which were actually distributed to her but the Commissioner ruled that she was also taxable upon the balance of the trust income (R. 3).

Upon review, the Board of Tax Appeals held such action of the Commissioner was erroneous but the court below reversed the decision of the Board.

ARGUMENT

Section 167 (2) of the Revenue Act of 1934 (Appendix, *infra*) provides that where any part of the income of a trust may, in the discretion of the grantor or of any person not having a substantial adverse interest in the disposition of such part of the income, be distributed to the grantor, then such part of the income of the trust shall be included in computing the net income of the grantor.

The court below held, correctly, we submit, that the excess income which was distributable to the grantor in the discretion of the husband-trustee was so distributable by a person not having an adverse interest and that it was, therefore, taxable to the grantor under Section 167. In so holding, the court indicated that in view of the family relationship and the sound financial circumstances of the husband and wife and their minor son, there was no adequate basis for concluding that the trustee had an interest substantially adverse to his wife merely because he could use accumulated income for the future support of the boy in case of necessity. (R. 9–12.) Cf. *Loeb* v. *Commissioner*, 113 F. (2d) 664 (C. C. A. 2d), certiorari denied, 311 U. S. 710; *Fulham* v. *Commissioner*, 110 F. (2d) 916 (C. C. A. 1st); *Altmaier* v. *Commissioner*, 116 F. (2d) 162 (C. C. A. 6th), certiorari denied, March 31, 1941, No. 774, October Term, 1940.

In support of her application for a writ of certiorari, the taxpayer urges that the trustee was le-

gally obligated to support his minor son (*In re Ganey*, 93 N. J. Eq. 389, 394, affirmed, 94 N. J. Eq. 502), as well as his mother and other blood relatives (New Jersey Revised Statutes, 1937, Title 44: 1–140) for the benefit of whom he had discretionary power to use trust income. But that obligation was neutralized by an equal, if not greater, obligation to support his wife, the grantor (*Sobel* v. *Sobel*, 99 N. J. Eq. 376, 378–379; *Bochm* v. *Bochm*, 88 N. J. Eq. 74, 78–79). Accordingly there is no basis for the conclusion that he would be interested in withholding the income from his wife in order to devote it to others. Furthermore, the wife was manifestly interested in the welfare of her son and the other relatives to whom distributions might be made. Viewing the situation realistically, as did the court below, there seems little basis for any conclusion that the husband would not have dealt with the income here involved in accordance with the wishes of his wife and it seems clear that "the scheme which the taxpayer now urges for the trust" (R. 12) is no more than a means whereby she might contribute to her son's estate and to relatives without liability for tax on the income thus indirectly devoted by her to such purposes. Cf. *Helvering* v. *Horst*, 311 U. S. 112; *Harrison* v. *Schaffner*, decided March 31, 1941, No. 437, October Term, 1940. In these circumstances the court below correctly concluded that the husband did not have a "substantial adverse interest" in the income

and that the grantor was therefore properly chargeable therewith under Section 167.

CONCLUSION

The decision below is correct. It turns upon the peculiar facts of the case and does not present a question of general importance. There is no conflict. The petition should be denied.

Respectfully submitted.

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JULY, 1941.

APPENDIX

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 167. INCOME FOR BENEFIT OF GRANTOR.

(a) Where any part of the income of a trust—

(1) is, or in the discretion of the grantor or of any person not having a substantial adverse interest in the disposition of such part of the income may be, held or accumulated for future distribution to the grantor; or

(2) may, in the discretion of the grantor or of any person not having a substantial adverse interest in the disposition of such part of the income, be distributed to the grantor; or

(3) is, or in the discretion of the grantor or of any person not having a substantial adverse interest in the disposition of such part of the income may be, applied to the payment of premiums upon policies of insurance on the life of the grantor (except policies of insurance irrevocably payable for the purposes and in the manner specified in section 23 (o), relating to the so-called "charitable contribution" deduction); then such part of the income of the trust shall be included in computing the net income of the grantor.

(b) As used in this section, the term "in the discretion of the grantor" means " in the

discretion of the grantor, either alone or in conjunction with any person not having a substantial adverse interest in the disposition of the part of the income in question." (U. S. C., Title 26, Sec. 167.)

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

> ART. 167–1 [as amended by T. D. 4759, 1937–2 Cum. Bull. 117, 118, and T. D. 4860, 1938–2 Cum. Bull. 184]. *Trusts in the income of which the grantor retains an interest.*—(*a*) *Scope.*—Section 167 prescribes that the income, or any part of the income, of certain trusts shall be taxed to the grantor, not because the grantor has retained a certain interest in the *corpus* of the trust (as in section 166), but because of his retention of a certain interest in the *income* of the trust. This article deals with the taxation of such income. The term "income," as used in this article, means any part of the whole of the income of the trust.
>
> (*b*) *Test of taxability to the grantor.*—The test prescribed by the Act as to the sufficiency of the grantor's retained interest in the trust income, resulting in the taxation of such income to the grantor, is whether he has failed to divest himself, both permanently and definitively, of every right which might, by any possibility, enable him to have such income, at some time, distributed to him, either actually or constructively. Such a distribution to the grantor occurs within the meaning of section 167 if the income is paid to him or to another in obedience to his direction or if the income is applied in payment of premiums upon policies of insurance on the grantor's life.
>
> For the purposes of this article, the sufficiency of the grantor's retained interest in

the income is not affected by the fact that the grantor has provided that the right to so effect or direct the distribution of income is, or may at some future time be, vested in any person (either alone or in conjunction with the grantor) not having a substantial interest in the income adverse to the grantor.

If the grantor has retained any such interest in the income, such income is taxable to the grantor regardless of—

(1) whether it may be distributed currently or accumulated for future distribution;

(2) whether such distribution, either current or subject to accumulation, is fixed by the trust instrument or is dependent on an exercise of discretion;

(3) whether, if such distribution is in any way effected by or dependent on an exercise of discretion, the person exercising the discretion is the grantor or a person not having a substantial interest in the income adverse to the grantor, or both. A bare legal interest, such as that of a trustee, is never substantial and never adverse;

(4) the time or times of such distribution, whether within or without the taxable period, whether conditioned on the precedent giving of notice, or on the elapsing of an interval of time, or on the happening of a specified event, or otherwise;

(5) when the trust was created.

Thus the inclusion of any trust within the scope of section 167 is based on the fact that the grantor has retained an interest in the income therefrom by which he is, or may be enabled at some time, to receive its benefits. But the provisions of section 167 are not to be regarded as excluding from taxation to the grantor the income of other trusts, not specified therein, in which the grantor is, for

the purposes of the Act, similarly regarded as remaining in substance the owner of the trust income. If, for example, trust income is applied in satisfaction of the grantor's legal obligation whether to pay a debt, to support dependents, to pay alimony, to furnish maintenance and support, or otherwise, such income is in all cases taxable to the grantor.

If the grantor strips himself permanently and definitively of every such interest retained by him, the income of the trust realized after such divesting takes effect is not taxable to the grantor but is taxable as provided in sections 161 and 162.

A person may have an interest that is both substantial and adverse to the grantor in the disposition of only part of the income. There is to be excluded in computing the net income of the grantor only that part of the trust income in the disposition of which such person has a substantial interest adverse to the grantor.

(*c*) *Income and deductions.*—If, as to any of the income, the test of taxability to the grantor is satisfied, such income shall be included in the gross income of the grantor, and he shall be allowed those deductions with respect to such income as he would have been entitled had such income been distributable currently to him.

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